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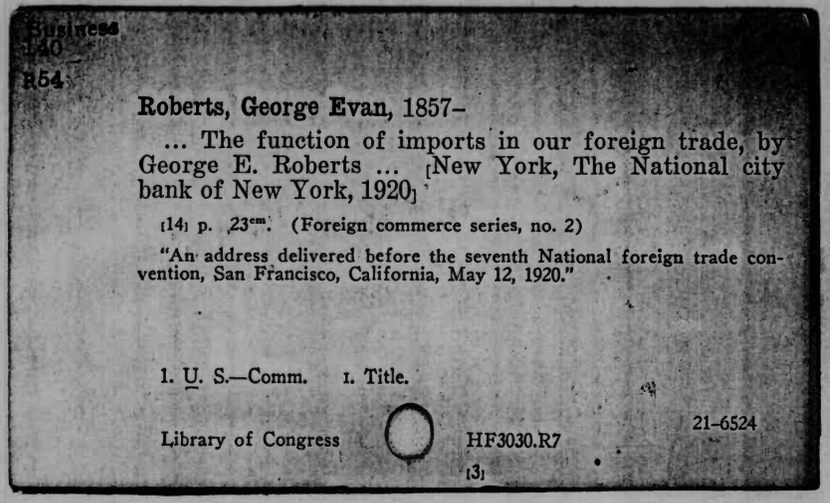

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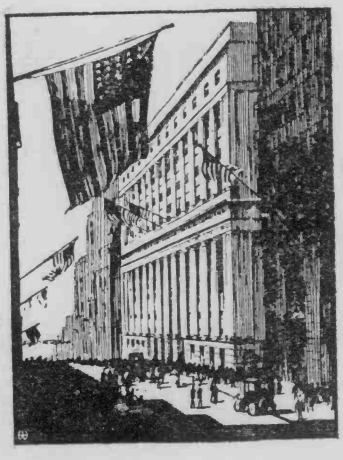

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THE FUNCTION OF IMPORTS IN OUR FOREIGN TRADE

THE great War has brought about certain changes of a fundamental character affecting trade and financial relations between the United States and other countries, and those changes must be fully comprehended if we are to plan intelligently for the future. Our trade relations in the past have developed in harmony with our past position as a borrowing nation, a debtor nation on account of foreign investments. We were a new country of vast undeveloped resources, affording opportunity for cheap production of foodstuffs and raw materials, of which the world, and particularly the countries of Europe, were in need. Our population grew rapidly by immigration from Europe, and, in the earlier years of our development, from the countries of Europe most advanced in the arts of industry and in accumulations of capital. It was natural under these circumstances and with the development of steam power in transportation, that capital should flow freely from Europe to this country for investment, and the earnings of this capital, unless reinvested here, were a charge against us in the international exchanges.

Equilibrium of Exchange

THIS situation existed not only in the early years of development, but up to the outbreak of the War. European holdings of our securities were largely increased in the period of expansion which began about 1900. During the ten years next preceding the outbreak of the War the average annual balance of trade in favor of the United States on merchandise account was approximately $500,000,000, and it was practically offset by the balance in what has been called the invisible account—in other words, by interest and dividend payments upon American securities held abroad, charges of foreign shipping against our commerce, earnings of foreign insurance companies in this country, commissions of foreign bankers, expenditures of American tourists abroad, remittances of our foreign-born residents to relatives in the old countries, etc.

It is evident that the War has disturbed this old state of equilibrium. We have bought back most of the American securities which were held abroad and the interest and dividends upon them here-

after will remain at home. We are building a great fleet of merchant ships with the intention of carrying a larger portion of the over-seas trade, and we have become creditors to Europe in a very large amount. Including the loans of the United States Government to the governments associated with it in the War, the balance in our favor upon interest account is doubtless considerably above $500,000,000 per annum.

Transfer of "Invisible" Account Balance

WHAT effect will this shift of the balance of payments in the "invisible" account have upon our foreign trade? How many people have realized that there is a relationship between the two classes of payments, or that they have influence upon each other? And yet a moment's reflection will show that the payments and receipts of a country in international relations must balance in the aggregate. Nothing is given away. Eager as everybody is for trade, nobody wants to sell unless he receives in some form what he considers an equivalent; and a country which is a debtor on capital account must not only pay for all the goods it imports but keep up its interest payments besides. It follows, therefore, that a borrowing country normally exports more commodities than it imports and that a lending country normally imports more than it exports. "Normally" in this case means "in the long run" and without taking account of new lending operations.

In the past it was necessary for the United States to have a trade balance of approximately $500,000,000 per year in order to pay the charges accruing against it abroad; but in the future it will be necessary for the United States to have a balance of perhaps an equal amount in its favor in order to collect the interest running in its favor and against other countries.

Debtor Country Must Have Favorable Trade Balance

THIS may sound to some people like a startling and even alarming change. Our own history has accustomed us to thinking that we must have a trade balance in our favor in order to be in a sound and prosperous condition, but that was true because we were in a debtor position. We had to have an excess of exports over imports sufficient to meet the other charges in the account against us, or we

had to settle the difference in gold or securities, and if gold was withdrawn from our bank reserves for the purpose it meant a contraction of credit, a check to enterprise and probably a period of falling prices and business depression. Our belief in the necessity for a favorable trade balance has been based upon our own experience that good times came with the trade balance and that bad times came when the balance turned against us, but we must now consider that our position is reversed, that our own requirements are reversed, and that the countries which are now debtor to us need to have the favorable trade balance for the same reason that we formerly required it. It is in the interest of both sides that the debtor country shall have the favorable trade balance, because that is the only condition under which it can meet its obligations.

Europe's Debt to Us Cannot Be Settled in Gold

AS BETWEEN individuals there are only three ways in which a settlement can be made. You pay in cash, or you pay in trade, or you give your note, which of course is not a final settlement, but a postponement to a more convenient time. As between nations the situation is just the same. You pay in gold, which is the cash of international transactions, or you pay in trade, or you pay in securities which are evidence of continuing obligations. Now, we know that foreign countries will not be able to pay us in gold, for the total production of gold in the world outside of the United States is less than $400,000,000 per year, and even if the debtor countries were able to send us considerable sums in gold, the effect would be to cause a further inflation of prices in this country, which would be to our disadvantage in foreign trade and an injury to us at home. It would be idle and unintelligent for us to meet in conventions and plan to build up a great export trade expecting to collect the proceeds in gold.

We have done too much of this in the past. We have given all our thought to exports, to selling our products in other countries, without considering how the foreign customers we are seeking will be able to make payments for their purchases. That problem is just as much ours as theirs, for they cannot solve it without our help, and they cannot buy unless they are able to render reciprocal services to us.

How a Foreign Purchaser Makes His Payment

IN NORMAL times an exporter gives little attention to how a foreign purchaser will make payment. He turns his foreign drafts over to his banker and gets credit for them, with scarcely a thought as to the means by which these drafts are settled. He doesn't realize that they are paid with the proceeds of foreign products coming into the country. The services of the banker relieve him of the necessity of personally arranging the barter of his goods in foreign markets, but fundamentally trade is barter and it must be thought of as such to understand it.

Nothing but the disorganized state of industry in Europe and the pressing necessities of the world enable our exports to continue as at present. They buy of us because there is no alternative. But the world will not remain forever in its present state. Gradually order will be restored, production will be resumed and business will get back to a competitive basis. We must consider what our position will be when that time comes.

"Favorable Exchange" Really Unfavorable to Our Exporters

WE HAVE been accustomed to say that the exchanges are in our favor when the dollar rates above the other currencies. They *are* in our favor in the sense that for the moment we are selling more than we are buying, and that the dollar holds the commanding position in the markets of the world. They are in our favor for buying purposes; they are in our favor for importing purposes, but they are not in our favor for selling purposes. Dollar drafts at a premium mean that American goods cost more to foreign customers; a premium upon dollar exchange is an obstacle to our export trade which we will be compelled to reckon with.

The case of our neighbor, Canada, affords an opportunity to study the effects of an unbalanced trade, and to observe the influences which naturally come into play to restore the balance. The balance in favor of the United States in trade with Canada in three years has averaged over $300,000,000 per year. If the total of all payments running each way were the same, the drafts drawn in each country on the other would meet in the clearing houses and offset each other, and exchange would be at par. But with these

heavy balances running against Canada there is need for Canadians to make greater payments in the United States than the credits created by their exports will cover.

IF Canada has balances in her favor in trade with other countries, but those countries also are in debt to the United States, so that those balances cannot be used for settlement here. Under ordinary conditions, the Canadian banks would ship gold, but the total gold reserves of Canada are not much above $200,000,000, and the reserves might be drained entirely away.

Result of Canada's Demand Upon Us

THE situation is that there is a greater demand in Canada for means of making settlements in the United States than can be readily satisfied, with the result that exchange has been forced to a premium. In the fall of 1918 the premium was about 2 per cent, in the spring of 1919 it was about 3 per cent, in the early fall of 1919 it was 4 per cent, in November it was 5 per cent, in January, 1920, it was 10 per cent and in February it was 15 per cent. This premium is not fixed in the United States; it results from competition in Canada for the means of payment in the United States. It is not a reflection upon the credit of Canadian traders; the Canadian purchaser may have ample funds with his own bankers to make the payments. It is not a reflection upon Canadian bankers or Canadian money. Canadian Government credit is not involved at all. It is not a situation caused by bankers or that can be remedied by bankers. The situation arises from a state of one-sided trade, and from the difficulty under such conditions of making payments in another country and a different currency.

The premium is an open offer to anyone who will come forward and provide means of payment in the United States. It amounts to an inducement in the nature of a bounty for Canadians to export products to the United States and sell the exchange thus created. The Canadian paper and pulp manufacturers are making a handsome additional profit on their sales in the United States by selling their American drafts at a premium.

And while it encourages exports from Canada to this country it burdens and discourages exports from this country to Canada. The

Canadian purchaser of American goods must pay the price in this country and then pay a premium of 10 or 15 per cent to obtain the means of payment.

Importance of Canada as Our Customer

CANADA, among all countries, next to Great Britain, is the best customer for American goods, but the Canadians cannot buy without the means of paying. Our trade is being curtailed, partly by the added cost resulting from the exchange rates and partly by a deliberate policy. There is public agitation in Canada against any purchases in the United States except of goods that are indispensable, and talk of an embargo.

Our exporters are dealing with the situation as best they can. Some of them are dividing the cost of exchange with their Canadian customers, some of them are accepting pay in Canadian funds, and converting those funds into Canadian securities or other permanent investments on that side of the line, which is all right if they can spare the capital from their business. Others have abandoned the Canadian trade. All of the foregoing expedients are of only temporary value. If the balances continue to pile up, the exchange situation inevitably will grow worse. There is no stopping point until the balances cease to accumulate.

I use the case of Canada as an illustration because the situation there is clearly the result of an unbalanced trade. Exchange rates with some of the countries of Europe are affected by inflated and depreciated currencies, but while there is doubtless a degree of inflation in Canada we cannot say there is any more than in the United States. The situation as to the two countries therefore affords a clear demonstration of the effect of a one-sided trade upon exchange rates and of the vital part which exchange rates play in foreign trade.

Factors That Will Bring Our Foreign Trade into Balance

THE plain truth is that if in our relations with the rest of the world the balance of payments runs continually in our favor, both on trade account and on interest account, exchange rates will rise against us as the balances increase, discouraging exports and encouraging imports, until the trade is brought substantially into balance.

Every situation like this brings a lot of people to the front with remedies. There are proposals for an international currency, an international gold reserve, an international clearing house, an international bank and for a Government foreign bank on our own account. All of these proposals overlook the fundamental truth that trade is essentially barter and in the long run must settle itself. Gold is a convenient medium for settling balances which run one way for a few months and the other way for a few months, but international trade is on such a great scale that the amount of gold available for payments is small in comparison. There isn't gold enough in all Europe to pay its adverse trade balance with the United States last year. Moreover, no country will allow its banking reserves to be disturbed unduly. We ourselves would be as quick as any to establish an embargo if our gold reserves were seriously threatened. The plain fact is that in the nature of things trade must be kept on the basis of barter; it must be brought into balance, and high exchange rates are the natural and only effective means of bringing it into balance.

A New Economic Situation

WE ARE confronted then with a new economic situation, which we are bound to recognize. We must give attention as good merchants to the conditions which confront our would-be customers and the means which they possess for making payments. The purchasing power of every country is in its own powers of production, and unless it can use those powers and market the products of its industries, it will not be in position to pay or buy. The whole scheme for which this Association is organized, the promotion of foreign trade, might as well be abandoned, unless we are ready to consider the development of real trade, the exchange of our products for the products of other peoples.

It is a mistake for us to advocate foreign trade, as is sometimes done, on the ground that we have so greatly increased our general productive capacity that we cannot consume the output of our industries. That is not true in a general sense, including all the industries. The people of the United States could easily consume a volume of production equivalent to twice the present industrial capacity of the country, provided production was adjusted and

balanced to their wants. Everybody would like to have twice as much house-room, an automobile, or two automobiles, and other things in keeping. There is no limit upon our ability to consume; the limit is on our ability to produce. But in some lines of production we have developed our capacity beyond the demands of our people for those products, and we want to exchange such products for other things of which we are in need. We cannot dispose of them, or use that industrial capacity, except on a basis of exchange. That is the real situation as to foreign trade.

Proposal for Greater Liberality Toward Imports

NOW WHAT are we going to do about it? And, particularly, what will be the attitude of associations like this, organized for the promotion of foreign trade? The subject undoubtedly presents some difficulties. A proposal to adopt a policy of greater liberality toward imports than this country has maintained habitually in the past will run counter to the long-established views of many people, arouse apprehensions and perhaps create some dissension even within the Association itself, but the question must be dealt with, one way or the other. An argument can be made for a policy of exclusion and isolation, keeping out all foreign products which are competitive in any degree with our own and restricting our exports correspondingly; and another argument may be made in favor of a more liberal policy which will afford an opportunity for a larger development of trade on mutually advantageous lines; but no well-supported argument can be made in favor of trying to expand our exports without increasing our imports. That is a waste of energy; it simply cannot be done. We must choose a consistent course.

America's Opportunity in World Markets

IN MY opinion it is inconceivable that the people of the United States will adopt permanently a policy which lays all emphasis upon being self-contained and which would restrict and handicap those industries which are able to compete in all markets, for the sake of other industries which do not have like possibilities of growth. The largest possibilities for the country lie in the industries which can make their way in world markets. The genius of our people will not be satisfied without a chance in the markets of the world. The facilities for travel and transportation are such that it is inevitable that trade shall reach across national boundaries, and it is favorable to national efficiency and development and in the common interest of industrial progress that this shall be the case. In saying this, however, I am not making a declaration in favor of any radical change from the policy which is embodied in our laws today. Nothing should be done that will change materially the position of the great essential industries of the country in which thousands of people are employed and millions of capital are invested. It is not desirable to unsettle these industries, and to a great extent they are quite secure in their own strength.

Industry is undergoing constant changes, the volume of trade is rapidly increasing, and if we are guided in the future by recognition of the reciprocal nature of all permanent trade it is not likely that tariff changes materially affecting existing industries will need to be made.

A Creditor to Europe—a Debtor to South America

WE ARE in the debtor position on trade account toward South America and Asia, and in a creditor position toward Europe, Africa and the other countries of North America. Conditions are unfavorable to an expansion of our exports to Europe and Canada, but favorable to such expansion in South American and Asia, providing we continue to receive the products of the latter upon present terms. These products are mainly foodstuffs and raw materials which are required in our industries and they come into competition with our own products only in the sense that the domestic supply is insufficient to meet our wants. Wool and hides are examples of these products. There is no reason to believe that the domestic supply of these commodities can be made equal to our needs, and that being true it follows that any charges which may be laid upon our importations will raise the level of costs for our entire consumption, and tend to put the industries dependent upon these materials at a disadvantage in competition with foreign rivals.

Receiving Raw Materials on Free Basis

THE general level of prices for foodstuffs and raw materials has risen so much all over the world that there seems to be no occasion

for raising them higher in this country by artificial means. The great rise of farming land values in this country in the last twenty years indicates that the prices of farm products have been generally on a remunerative basis. Although they may decline to some extent, it is generally agreed that they will not fall to pre-war prices.

We are now receiving foodstuffs and raw materials, which are the principal products of South America and Asia, practically on a free basis, and it is in the interest of our export trade to those quarters that this status should not be altered. These are hopeful fields for an expansion of our exports, but they will not be if we set up obstructions to the natural flow of their products to our markets.

Any duties laid upon this class of imports will come back in full measure upon the entire population and be a handicap to the exporting industries which use them.

Market Here for Foreign Investments

IN CONCLUSION, it should be said that the readjustments incidental to our transition from the conditions of a debtor country to those of a creditor country may be greatly eased and facilitated by the development in the United States of a market for foreign investments. It is understood that the interest running on the outstanding obligations of foreign governments to the United States Government will be funded for several years, and therefore will not in the meantime affect the exchange situation. If our people will take a lesson from the history of the upbuilding of the great foreign trade of Great Britain and Germany, they will take advantage of low exchange rates to secure permanent investments which will be helpful to trade in the future. Both of these countries have played a large part not only in the expansion of international commerce but in the increase of world production, by supplying capital in the form of industrial equipment for the countries of undeveloped natural resources. They kept exchange rates from rising against them by admitting freely the products of the countries where they were building up their exports and by re-investing in part the income derived from those countries for further expansion of their interests

National Prosperity in Balanced Trade

THESE are the policies which have brought success to the countries that have preceded us in the development of world trade. They will be practising the same methods in the future, studying the needs and interests of the people whose trade they are seeking. We can have success upon the same terms, but upon no other. In the long run and taking the large view, the greatest prosperity for every country is to be found in such a balanced and mutually-supporting state of international trade as stimulates industry and prosperity everywhere.

This is a fundamental proposition which in its broad significance cannot be controverted, but in the eagerness of individuals to sell and amid the apprehensions which arise from vigorous competition, the people of every country are prone to overestimate the dangers which threaten them from the competition of other countries. It is possible for one country, by reason of natural advantages or by painstaking efforts, to obtain a dominant position in a single industry, but the same reasons which prevent a great one-sided trade in favor of the United States likewise forbid such a trade in favor of any other country. It is impossible for any country to monopolize the trade of the world. Great Britain always has imported more commodities than she exported. Germany was increasing her foreign trade rapidly, but for the five years preceding 1914 her imports exceeded her exports.

Production the Measure of Buying Power

THE people of no country can do more than work all the time, and however efficient they may be in production they will not be able on the whole to do any more than supply their own wants, because their wants will develop as fast as their production, which is the measure of their buying power. It does not follow that they will supply all their own wants directly; they never do that; a country naturally sends abroad a part of its production in exchange for the production of other countries, but the population of every country will gladly consume the equivalent of its own production, and in the long run is bound to do so.

I have had friends express great concern to me about the future competition of different countries; sometimes it has been Great

Britain, sometimes it has been Germany; sometimes it has been Japan. Any of these countries may specialize in certain industries and become formidable competitors in them, but nothing is more certain than that none of these countries in any general sense can crowd other countries out of industry. None of them in the long run will sell any more than it buys or make in the aggregate any more commodities than it consumes. None of them will make goods for other countries without wanting something in return.

Bogey of "Cheap Japanese Labor"

JAPAN is sometimes mentioned as a threatening competitor because of the low wage rates prevailing there, but wages are low in Japan because the machine equipment of the country has been small and the productive capacity of the country has been small. Japan can hardly produce enough to satisfy the growing wants of her own people. Their consumption and their wants will keep pace with any increase in productive capacity that they can accomplish. Their imports grow as fast as their exports, and so it is everywhere.

One of the grievances alleged against the labor organizations is that they sometimes limit the output, acting upon the theory that there is only a limited amount of work to be done, and that it is to their interest to make it go as far and pay as much in wages as possible. Every such conception of industry and business is fundamentally wrong. There is no limit to the amount of work to be done or the amount of business to be had, because there is no limit to the amount of wealth that may be created from the natural resources or to the consumptive demands of the world's population.

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